Jardine Lloyd Thompson Sdn Bhd v Berjaya Sompo Insurance Bhd

HIGH COURT (KUALA LUMPUR) — CIVIL SUIT NO 22NCC-97–01 OF 2013

NALLINI PATHMANATHAN J

27 AUGUST 2013

Insurance — Insurance broker — Liability under policy — Indemnity against any claim — Insurance broker defrauded by employee — Overpayment of insurance premiums taken out by bank — Notification of potential claim under policy — Liability to indemnify losses suffered as consequence of employee's fraudulent actions

The plaintiff was a company carrying on the business of providing general insurance and life insurance broker while the defendant was a company which carried on the business of underwriting general insurance for brokers such as the plaintiff. Vide a policy of insurance ('the policy'), the defendant agreed to indemnify the plaintiff for the period from 1 January 2012 to 31 December 2012 against any claim which might be made against the plaintiff. The plaintiff's client, Affin Bank Bhd ('the bank') had been defrauded or cheated by one of the plaintiff's then employees ('Razak'), into overpaying on certain insurance premiums taken out by the bank with the plaintiff. There were seven separate payments made by way of cheques issued by the plaintiff to three different event management companies under the mistaken belief that it was for further management programs. The same monies were then transmitted via the plaintiff's account to third party accounts, at the behest of Razak. The bank lost monies because there was in actuality no risk management programs as held out by Razak. The bank demanded an accounting of the fraud/deception and notified the plaintiff of its intent to issue a claim against the plaintiff for the return of all sums of monies that had been overpaid. These were the monies that were misappropriated by Razak. The plaintiff therefore notified the defendant of a potential claim under the policy. The plaintiff contended that by virtue of the policy, the defendant was liable to indemnify the plaintiff for the loss it suffered as a consequence of Razak's fraudulent actions in the sum of RM1,096,372.01. However, the defendant repudiated the claim on the grounds, inter alia, the claim did not fall within the Option 1 - Amendment of Dishonesty Exclusion which was an optional extension under the policy and which excluded the applicability of exclusion cl 1(b) in the policy. The issues that arose for the court's determination were: whether the loss of monies claimed by the plaintiff fell within the optional extension clause of the policy;

and whether the payments to the individual event management companies fell within the optional extension clause of the policy.

Held, dismissing the claim:

(1) The optional extension clause would serve no useful purpose if the proviso to it were accorded its normal and natural meaning which would be to exclude financial loss, which was the loss suffered by the plaintiff in the instant case. The proviso ought simply to be accorded its natural and ordinary meaning, so as to exclude loss of monies arising out of the dishonest acts of employees of the plaintiff. Optional Extension cl 1 certainly provided cover or indemnification for dishonest acts of the plaintiff's employees. However such cover was expressly subject to the proviso that it did not cover claims for loss of money, negotiable instruments, bearer bonds or coupons, stamps, bank or currency notes (see paras 56–58(a)).

(2) If the parties had intended to cover only physical loss of monies or financial instruments, then this should have been and would have been clearly stipulated. There was a considerable difference between 'loss' and 'physical loss'. The latter envisaged that the money or financial instrument was lost or misplaced or disappears. However 'loss' encompassed a wide variety of events including a shortfall or deficiency or debit or deficit of money albeit from theft of monies or loss of a financial benefit by reason of the loss of a financial instrument, rather than the physical loss of the instrument itself. Loss also routinely encompassed damage and injury in a variety of insurance policies. Given the wide discrepancy between the definitions, it would have been incumbent upon parties to specify that loss was restricted to a physical loss. The insertion of the word 'physical' could not be justified as an 'implied' term under the commercial necessity test or the official bystander test (see para 58(d)–(e)).

(3) Whether the loss was considered as having arisen at the point when the bank made the payments to the plaintiff or the monies were diverted from the plaintiff into third party accounts by the dishonest machinations of Razak, the loss was a financial loss. The financial loss was suffered by the bank and was reimbursed by the plaintiff. This claim was therefore a claim arising from financial loss suffered by a client in respect of which it sought reimbursement from the plaintiff as the financial loss arose by reason of the dishonest acts of the plaintiff's employee. However, it could not be disputed that at all times the basis of the claim was a loss of monies brought about by the dishonest conduct of Razak. These payments to the individual event management companies which was part of the fraud or modus operandi utilised by Razak, fall within the proviso to Optional Extension cl 1, being a loss of monies (see paras 61–62).

[Bahasa Malaysia summary

Plaintif merupakan syarikat yang menjalankan perniagaan menyediakan insurans am dan broker insurans nyawa manakala defendan merupakan syarikat yang menjalankan perniagaan menaja jamin insurans am untuk broker-broker seperti plaintif. Melalui satu polisi insurans ('polisi tersebut'), defendan telah bersetuju untuk melindungi plaintif untuk tempoh dari 1 Januari 2012 hingga 31 Disember 2012 terhadap apa-apa tuntutan yang mungkin dibuat terhadap plaintif. Pelanggan plaintif, Affin Bank Bhd ('bank tersebut') telah ditipu oleh salah seorang daripada bekas pekerja plaintif ('Razak'), untuk membayar lebih premium insurans tertentu yang telah diambil oleh bank dengan plaintif. Terdapat tujuh bayaran berasingan yang dibuat melalui cek yang dikeluarkan oleh plaintif kepada tiga syarikat pengurusan acara berbeza yang telah salah tanggap bahawa ia adalah untuk program-program pengurusan seterusnya. Wang sama kemudian telah dipindahkan melalui akaun plaintif kepada akaun pihak ketiga, atas arahan Razak. Bank tersebut telah hilang wang itu kerana sebenarnya tiada program-program pengurusan risiko yang diadakan oleh Razak. Bank tersebut menuntut perakaunan penipuan/penipuan dan memaklumkan plaintif hasratnya untuk mengeluarkan tuntutan terhadap plaintif bagi pemulangan semua jumlah wang yang telah terlebih bayar itu. Wang tersebut telah disalahgunakan oleh Razak. Plaintif dengan itu telah memberitahu defendan tentang potensi tuntutan di bawah polisi tersebut. Plaintif berhujah bahawa menurut polisi tersebut, defendan bertanggungjawab untuk membayar plaintif untuk kerugian yang dialaminya akibat daripada tindakan penipuan Razak berjumlah RM1,096,372.01. Walau bagaimanapun, defendan menyangkal tuntutan tersebut atas alasan, antara lain, tuntutan tersebut tidak terdangkum di bawah Option 1-Pengecualian Pindaan Ketidakjujuran yang merupakan lanjutan pilihan di bawah polisi tersebut dan yang mengecualikan pemakaian pengecualian fasal 1(b) dalam polisi tersebut. Isu-isu yang timbul untuk ditentukan mahkamah adalah: sama ada kerugian wang yang dituntut oleh plaintif terangkum di bawah fasal lanjutan pilihan kepada polisi tersebut; dan sama ada bayaran kepada setiap syarikat pengurusan acara terangkum di bawah fasal lanjutan pilihan kepada polisi tersebut.

Diputuskan, menolak tuntutan:

(1) Fasal lanjutan pilihan tidak mempunyai tujuan yang berguna jika proviso kepadanya memberikan maksud biasa dan semulajadinya yang mana adalah untuk mengecualikan kerugian kewangan, yang merupakan kerugian yang dialami oleh plaintif dalam kes ini. Proviso tersebut patut hanya memberikan maksudnya yang semulajadi dan biasa agar mengecualikan kerugian wang yang wujud daripada tindakan penipuan pekerja-pekerja plaintif. Lanjutan Pilihan fasal 1 sememangnya memberikan perlindungan atau penanggungan kerugian untuk tindakan penipuan oleh pekerja-pekerja plaintif. Walau bagaimanapun

perlindungan sedemikian adalah jelas tertakluk kepada proviso tersebut bahawa ia tidak meliputi tuntutan untuk kerugian wang, surat cara boleh niaga, pembawa bon atau kupon, setem, nota bank atau matawang (lihat perenggan 56–58(a)).

(2) Jika pihak-pihak mempunyai niat untuk meliputi hanya kerugian wang secara fizikal atau surat cara kewangan, maka ini patut telahpun dan dengan jelas ditetapkan. Terdapat perbezaan jelas antara 'kerugian' dan 'kerugian fizikal'. 'Kerugian fizikal' membayangkan bahawa wang atau surat cara kewangan telah hilang atau salah letak atau lesap. Namun begitu 'kerugian' merangkumi pelbagai kejadian termasuklah kekurangan atau debit atau defisit wang walaupun daripada wang yang dicuri atau kehilangan sesuatu faedah kewangan oleh sebab kerugian instrumen kewangan, dan bukannya kerugian fizikal instrumen itu sendiri. Kerugian juga secara rutin merangkumi kerosakan dan kecederaan dalam pelbagai polisi insurans. Memandangkan perbezaan yang luas antara definisi-definisi tersebut, ia adalah penting bagi pihak untuk menyatakan bahawa kerugian adalah terhad kepada kerugian fizikal. Kemasukan perkataan 'fizikal' tidak mungkin dibenarkan sebagai istilah 'tersirat' di bawah ujian keperluan komersial atau ujian pemerhati rasmi (lihat perenggan 58(d)–(e)).

(3) Sama ada kerugian dianggap telah timbul apabila bank tersebut membuat bayaran kepada plaintif atau wang tersebut dialihkan daripada plaintif ke dalam akaun pihak ketiga oleh persekongkolan penipuan Razak, kerugian tersebut adalah kerugian kewangan. Kerugian kewangan tersebut dialami oleh bank tersebut dan telah dibayar balik oleh plaintif. Tuntutan ini oleh demikian adalah suatu tuntutan yang timbul daripada kerugian kewangan yang dialami oleh pelanggan yang telah memohon untuk bayaran balik daripada plaintif kerana kerugian kewangan yang timbul akibat tindakan penipuan pekerja plaintif. Walau bagaimanapun, ia tidak boleh dipertikaikan bahawa pada setiap masa asas untuk tuntutan adalah untuk kerugian wang yang disebabkan oleh tingkah laku Razak. Bayaran-bayaran kepada syarikat-syarikat pengurusan acara secara berasingan yang merupakan sebahagian daripada penipuan atau modus operandi yang dimulakan oleh Razak, terangkum di bawah proviso Lanjutan Pilihan fasal 1, iaitu kerugian wang (lihat perenggan 61–62).]

Notes

For a case on liability under policy, see 8(1) *Mallal's Digest* (4th Ed, 2013 Reissue) para 197.

Cases referred to

Malaysia British Assurance Bhd v Syarikat Pembenaan Karun Sdn Bhd [2008] 6 MLJ 533, CA (refd)

Perembun Consortium (a joint venture between Perembun (M) Sdn Bhd and Road Builder (M) Sdn Bhd) & Anor v AXA Affin General Insurance Bhd (fomerly known as AXA Affin Assurance Bhd) [2011] 6 MLJ 719, HC (refd)

Rouleston Clarke Pty Ltd (In Liquidation) v FAI General Insurance Company Limited [2000] TASSC 63, SC (folld)

Syarikat Uniweld Trading v The Asia Insurance Co Ltd [1996] 2 MLJ 160, HC (refd)

Legislation referred to

Rules of Court 2012 O 14A

KM Chan (Paul Ngooi with him) (Lim Kian Leong & Co) for the plaintiff. Satharubant (Korinavathi with him) (Satha & Co) for the defendant.

Nallini Pathmanathan J:

INTRODUCTION

[1] The plaintiff is a company carrying on the business of providing insurance and re-insurance broking services. In other words, it is a general insurance and life insurance broker. The defendant is a company which carries on the business of underwriting general insurance for brokers such as the plaintiff.

[2] Vide a policy of insurance under Policy No 12HDQ/LNDZ78662 dated 4 January 2012 ('the policy') the defendant agreed to indemnify the plaintiff for the period from 1 January–31 December 2012 against any claim which might be made against the plaintiff, and notified to the defendant during the stipulated period. (The policy is a professional indemnity policy.)

SALIENT FACTS

[3] The plaintiff discovered in or around 31 January 2012, that one of its clients, Affin Bank Bhd ('the bank') had been defrauded or cheated by one of the plaintiff's then employees, one Abdul Razak bin Abdul Ghani ('Razak'), into overpaying on certain insurance premiums taken out by the bank with the plaintiff. The bank had been induced to make these payments on the basis of fictitious risk management programs and falsified/forged documents and letters. Razak then managed to appropriate these payments by fraudulently diverting these funds which had been paid by the bank to the plaintiff, into third party accounts and thereafter taking possession of the same. It is not in dispute that as a consequence of Razak's fraudulent acts, the bank lost monies because there was in actuality no risk management programmes as held out by Razak. They were entirely fictitious.

THE MODUS OPERANDI OF RAZAK'S FRAUDULENT ACTS

[4] The plaintiff's employee, who was supposed to act on the bank's behalf in so far as the insurance premiums paid by the bank were concerned, betrayed the bank's trust by issuing false debit notes, in excess of premiums actually required. When the bank paid the inflated premiums pursuant to the false debit notes, the first part of the fraud was complete. In other words the first tranche of fraudulent acts on the part of the employee was inducing the bank to pay the inflated premiums.

[5] The next part of the fraud involved getting the plaintiff to release these monies that the bank had been wrongfully induced to pay, for the fraudulent employee's own use. This was done by falsely representing to the plaintiff that the bank wanted risk management programs which were to be paid from the excess monies in the trust account to third party event management companies. It is not in dispute, and in fact an admitted fact, that Razak issued forged letters purportedly on behalf of the bank instructing these fictitious Risk Management Programs, that resulted in these payments to these companies. It is not in dispute that the plaintiff would not have made these payments but for such forged letters.

[6] The plaintiff, believing that such was the case, proceeded to issue cheques for the same quantum of monies to third party event management companies controlled by, or to which the fraudulent employee had access. When the plaintiff issued such payments for the purported Risk Management Programs, Razak appropriated these monies. The circle of fraud was complete.

[7] In this case there were seven separate payments made by way of cheques issued ultimately by the plaintiff to three different event management companies. These monies had of course, in the first instance been paid by the bank under the mistaken belief that it was for further management programmes. These same monies were then transmitted via the plaintiff's account to third party accounts, at the behest of Razak.

THE BANK'S DEMAND FOR A RETURN OF THE MONIES IT WAS WRONGFULLY INDUCED TO PAY

[8] The bank demanded an accounting of the fraud/deception and notified the plaintiff of its intent to issue a claim against the plaintiff for the return of all sums of monies that had been overpaid. These were the monies that were misappropriated by Razak.

A NOTIFICATION TO THE DEFENDANT BY THE PLAINTIFF OF A 'CLAIM' UNDER THE POLICY

[9] The plaintiff therefore notified the defendant of a potential claim under the policy on 9 March 2012. The plaintiff maintains that by virtue of the policy, the defendant was and is liable to indemnify the plaintiff for the loss it suffered as a consequence of its then employee's fraudulent actions in the sum of RM1,096,372.01.

[10] The defendant however vide letter dated 2 May 2012 informed the plaintiff that it was repudiating the plaintiff's claim on several grounds namely:

(a) the plaintiff's claim did not arise from a negligent act, error, or omission committed by the plaintiff in the normal conduct of the plaintiff's profession as an authorised insurance broker as declared in the proposal form applying for the policy. The present claim, the defendant contended, did not fall within the ambit of the preamble of the policy. Further it was excluded by exclusion 10 of the policy which specifies that there is no indemnity coverage in respect of a claim by the plaintiff which is not assumed in the normal conduct of the plaintiff's profession as an insurance broker;

(b) the plaintiff failed to declare that it was engaged in businesses other than the business of a general insurance and life insurance broker, as a consequence of which the policy is rendered void for non-disclosure of a material fact;

(c) the monies paid out by the plaintiff to its client were an 'overpayment' which is not a claim that falls within the indemnity provided by the policy;

(d) the claim was the result of the dishonesty of the plaintiff's employee in extracting monies from the plaintiff's bank account and is therefore excluded by exclusions 1(b),(d) and (f)(ii) in the policy; and

(e) *the claim does not fall within the Option 1 — Amendment of Dishonesty Exclusion which was an optional extension under the policy and which excluded the applicability of exclusion cl 1(b) in the policy.* (Emphasis added.)

[11] Ultimately only issue (e) arises for consideration in this suit as the other matters were abandoned by the defendant.

[12] Notwithstanding the defendant's response, the plaintiff did, on 18 June 2012, make good to the bank, the payments that the bank had been wrongfully induced to make in the sum of RM1,096,372.01.

[13] The plaintiff then wrote to the defendant on 19 June 2012 expressing dissatisfaction with the defendant's repudiation of their claim and seeking to recover the said sum of RM1,096,372.01 from the defendant under the policy. The defendant however maintained its stance vide letter dated 27 June 2012 stating further that it was not liable to make any payments to the plaintiff as the said policy is not triggered by claims for refunds of overcharged sums. Such refunds, the defendant maintained, did not amount to a demand for compensation of damages as provided under the policy, which is a professional indemnity policy.

THE TRIAL

[14] This matter was fixed for trial over three days from 8–10 May 2013. The plaintiff proposed to call four witnesses, and the defendant, one. On the day of the trial, parties, upon the proposal of the court, concluded that this was a case where the facts were not substantially in dispute. They sought to reduce the dispute to one of law. To this end the matter was adjourned to enable the parties to agree on the facts as far as was reasonably possible to ascertain whether or not the matter could proceed summarily without the need for oral evidence pursuant to O 14A of the Rules of Court 2012.

[15] After an interval the parties by consent advised the court that the matter could indeed be disposed of summarily by way of determination on a point or points of law. At the parties' behest therefore the following was duly recorded:

> Parties have agreed that they will try as far as possible to reduce this dispute to one of law. To that end the parties propose to have the facts agreed upon as far as possible.

[16] Parties agree as follows:

(a) the plaintiff's case against the defendant is premised on an indemnity under a policy of insurance, a professional indemnity insurance for insurance brokers dated 4 January 2012;

(b) the plaintiff made a claim under the aforesaid policy on 9 March 2012 in respect of a series of fraudulent acts by one of its employees, Razak bin Abd Ghani. The modus operandi of the fraud is as set out in questions and answers 9–16 of the witness statement of Low Choon Hoong. This is not in dispute;

(c) the issue of fraud is admitted;

(d) there were no risk management programmes organised by the plaintiff for Affin Bank Bhd;

(e) the defendant also withdraws paras 12 and 14–15. The defendant

however will pursue the defence of material non-disclosure as set out in para 13 save that the last sentence is deleted;

(f) Low Choon Hoong will provide a statutory declaration to the effect that the monies disbursed from a premium trust account and not the plaintiff's operating account. The issue of 'overpayment' will also be addressed in the statutory declaration; and

(g) paras 28 and 30–31 of the witness statement of Low Choon Hoong is not in dispute. This only goes to the fact of the quantum paid out. It does not impinge upon the construction issues before the court.

[17] As such the parties agree that the following issues of law arise for consideration by this court. The matter is therefore dealt with under O 14A:

Question 1: Whether the loss of monies claimed by the plaintiff as a result of the Risk Management Programs does or does not fall within the Optional Extension Clause of the Policy

Question 2: Whether the payments to the individual event management companies falls within the Optional Extension Clause of the Policy

Question 3: Does the plaintiff owe the defendant the duty to disclose that it carries on risk management programmes given that risk management programmes are part of general insurance and life insurance brokerage business?

Question 4: Was there material non-disclosure on the part of the plaintiff in failing to declare the risk management programmes in the proposal form, so as to render the Policy void?

[18] Having agreed on these questions of law the matter was adjourned to enable Low Hoon Choong to put in his statutory declaration on the matters stated above. The matter was fixed for submissions on the foregoing questions of law on 10 May 2013.

[19] On 10 May 2013 parties further advised the court that questions 3–4 relating to the defence of material non-disclosure was no longer in issue. In other words, these questions were withdrawn as was the defence of material non-disclosure. This left only questions 1–2 for the consideration of the court. These two questions are matters of pure construction of the relevant clauses of the policy and optional extension clause of the policy.

[20] Given the foregoing the only issues before the court are as set out in questions 1–2. I therefore propose to address those questions only in determining liability in this suit.

[21] The factual matrix setting out the precise mode employed by the

fraudulent employee, Razak, is set out in full in the witness statement of one Low Choon Hoong, the vice president of the plaintiff at paras 9–16. I do not propose to reproduce his evidence here as it is no longer in dispute between the parties that such a fraud was, in fact, perpetrated by Razak.

Question 1: Whether the loss of monies claimed by the plaintiff as a result of the risk management programs does or does not fall within the optional extension clause of the policy

[22] It is necessary to consider the relevant clauses in the policy as well as the optional extension clause of the policy to determine this issue.

THE POLICY

[23] The salient terms of the policy provide, inter alia, as follows:

> The Company agrees, subject to the following limitations, terms and conditions and subject to any policy endorsements:
>
> 1. To indemnify the Insured against any Claim which may be made against the Insured and notified to the Company during the period of insurance stated in the Schedule;
>
> (a) For actual or alleged breach of professional duty in the profession of Authorised Insurance Broker;
>
> By reason of any negligent act, error, or omission committed by the Insured in the conduct of the Insured's profession as an Insurance broker.
>
> *EXCLUSIONS*
>
> 1. This policy shall not indemnify the insured in respect of any Claim or Claims made against them:
>
> (a) …
>
> (b) Brought about or contributed to by the dishonest, fraudulent, criminal, malicious or deliberate act, error or omission of the Insured …; or
>
> (c) …
>
> (d) For loss of money, negotiable instruments (including shares), bearer bonds or coupons, stamps, bank or currency notes in the care or custody of the Insured; or
>
> (e) …
>
> (f) …
>
> (g) …

A (h) …

2. …

…

B 10 This policy shall not indemnify the insured in respect of any Claim or Claims made against them which relate to any duty or obligation assumed by the Insured which is not assumed in the normal conduct of the Insured's profession as an insurance broker

C OPTIONAL EXTENSION CLAUSE

[24] The plaintiff however had purchased from the defendant an option ('option') which excluded the application of exclusion 1(b) above, so as to cover losses arising from the dishonesty/fraud of their employees. In other words the D plaintiff paid additional premiums to obtain further coverage to exclude the effect of exclusion cl 1(b). The policy is therefore subject to Option 1 — amendment of dishonesty exclusion, the salient portion of which provides as follows:

E If a limit for this Extension is specified in the Schedule, Exclusion (b) shall not apply in respect of Claims for damages for breach of professional duty arising out of or contributed to by the dishonest, fraudulent, malicious or deliberate conduct of the Insured's employees (but not including any partner, director or controlling officer). However, no indemnity will be provided to any person committing or condoning such dishonest, fraudulent, malicious or deliberate act(s).

F This extension does not cover claims arising out of or in connection with for loss of money, negotiable instruments, bear bonds or coupons, stamps, bank or currency notes.

G CONSTRUCTION

[25] The scope and effect of the policy which is determined by the words set out above mean in effect that the defendant agrees, subject to the limitations, terms and conditions set out in the policy and policy endorsements, *to* H *indemnify or fully compensate the plaintiff insured in respect of any claim which may be made against the plaintiff for an actual or alleged breach of professional duty as an authorised insurance broker, arising from any act, error or omission committed by the plaintiff in the course of it carrying on or conducting its profession as an insurance broker.* (Emphasis added.)

I

[26] The policy goes on however to specifically exclude any liability for cover on the part of the defendant where the plaintiff's claim is brought about or contributed to by the dishonest, fraudulent, criminal, malicious or deliberate act, error omission of the plaintiff in its business (It also excludes liability for

any claim arising out or in connection with the physical loss of monies, negotiable insturments, bear bonds or currency notes in the custody of the Plaintiff.). In other words any act or omission which is dishonest, fraudulent, criminal or malicious and which gives rise to a claim is expressly excluded by this exclusion clause in the policy. The plaintiff, under the terms of the policy cannot therefore make claim for the fraudulent or criminal or malicious acts of its employees vis a vis its clients, for which the plaintiff would have to assume vicarious liability.

[27] In order therefore to obtain cover for acts of fraud or dishonesty, the plaintiff, paid out further premiums to purchase the optional extension clauses which include in Option 1, an amendment of the dishonesty exclusion in cl 1(b).

[28] This option as produced in full above provides that exclusion 1(b) 'shall not' apply to claims for damages for breach of professional duty arising out of, or contributed to, by the dishonest or fraudulent or deliberate conduct of the plaintiff's employee. In other words, Option 1 has the effect of negativing the effects of cl 1(b) to the extent set out in Option 1. In essence it allows the plaintiff to make a claim or seek indemnity for losses arising from the fraudulent, criminal or deliberate acts or omissions of its employees.

LIMITS TO THE EFFECT OF THE OPTION EXTENSION CLAUSE, OPTION 1

[29] It should be noted however, that this optional extension clause at Option 1, which excludes the effects of exclusion cl 1(b) of the policy, does *not* extend to acts of dishonesty or fraud committed by, or condoned by, the principal officers of the plaintiff.

[30] More significantly for the purposes of the instant case, this optional extension clause at Option 1 also expressly states that *the extension does not cover claims arising out of, or in connection with the loss of money*, negotiable instruments, bear bonds or coupons, stamps, bank or currency notes. (Emphasis added.)

[31] The issue before this court is whether the 'loss of monies' claimed by the plaintiff, arising from the fraudulent conduct of its employee in misappropriating monies (by collecting extra premiums from the bank for fictional Risk Management Programmes) falls within the purview of Option 1 of the optional extension clause in the policy.

THE PLAINTIFF'S STANCE

[32] The plaintiff submits that upon a true construction of Option 1 of the

optional extension clause it is evident that the defendant is to indemnify the plaintiff in respect of 'claims' for damages for a breach of professional duty arising from the fraudulent act of an employee, as is the case here. The plaintiff further submits that the essential ingredients of Option 1 of the optional extension clause are as follows:

(a) there must be a professional duty to the client (the bank here);

(b) there must be an act of an employee of the plaintiff insured; and

(c) such act must be dishonest, fraudulent, malicious or deliberate.

[33] These conditions have all been met as:

(a) the plaintiff insured did owe a professional duty to the bank;

(b) Razak, an employee of the plaintiff insured, perpetrated the subject act giving rise to the losses; and

(c) The act or conduct of the plaintiff insured's employee, Razak, was dishonest and fraudulent.

[34] Accordingly the plaintiff contends that the claim made by the plaintiff prima facie falls within the purview or ambit of Option 1 of the optional extension clause.

[35] With respect to the specific limitation to Option 1, namely that it does not cover claims arising out of a 'loss of monies', the plaintiff submits that the said extension has no application to the present factual matrix for the following reasons:

(a) the plaintiff expressly purchased this option to defeat the effect of the exclusion clauses in the first part of the policy. The plaintiff purchased the option so as to allow for claims arising out of the fraudulent or dishonest acts of its employees. To now contend that precisely such a loss as was sought to be covered under the optional extension clause (ie a loss caused by the dishonesty of an employee) is excluded by the use of the words 'loss of monies' in the proviso to that clause leads to an absurd construction or result. The plaintiff draws an analogy with the purchase of a third party motor insurance only to be told subsequently that no claims may be made thereunder because the loss involved money payments;

(b) the plaintiff submits that the only logical interpretation to be accorded to Option 1 of the optional exclusion clause including the proviso, is that the proviso or exclusion for loss of monies refers to a fidelity type of insurance that relates to cover for the loss of physical cash or cash equivalent from the insured's premises, based on the *ejusdem generis* rule; and

(c) the plaintiff further points that the well-established principle in insurance law that where two or more interpretations can be accorded to a contractual clause in an insurance policy the 'contra-proferentum' rule would come into play. The net effect of the rule would be to adopt the construction which goes against the insurer. In support of this proposition the plaintiff relies, inter alia, on *Perembun Consortium (a joint venture between Perembun (M) Sdn Bhd and Road Builder (M) Sdn Bhd) & Anor v AXA Affin General Insurance Bhd (fomerly known as AXA Affin Assurance Bhd)* [2011] 6 MLJ 719 and *Malaysia British Assurance Bhd v Syarikat Pembenaan Karun Sdn Bhd* [2008] 6 MLJ 533 (FC).

[36] Applying the same to the instant case, the plaintiff argues that two different interpretations have in fact been put forward to the court. On the one hand the defendant contends that the effect of the proviso is to exclude altogether any or all claims that relate to a loss of monies. The plaintiff on the other hand maintains that the term 'loss of monies' in the proviso to Option 1 of the optional extension clause refers only to financial losses arising from the loss of physical cash or its equivalent in terms of bearer bonds, shares etc. In light of the two contradictory definitions put forward the plaintiff urges the court to apply the *contra proferentum* rule and construe Option 1 of the optional extension clause in favour of the plaintiff.

THE DEFENDANT'S STANCE

[37] In essence the defendant submits that the exact words of the proviso to Option 1 of the optional extension clause must be given their clear and literal meaning. The defendant points to the express words of the proviso to Option 1 and maintains that the only meaning to be accorded to the proviso is that the defendant is not liable for claims arising out of or in connection with a loss of monies. The express words provide: 'This extension does not cover claims arising out or in connection with for loss of money, negotiable instruments, bear bonds or coupons, stamps, bank or currency notes.'

[38] The defendant does not dispute the fact that Razak acted dishonestly and that the loss suffered by the bank and therefore ultimately the plaintiff, arose by reason of the dishonest conduct of an employee. However the defendant points to the clear words of the exclusion clause and submits that the loss suffered by the bank, and ultimately the plaintiff in the course of its insurance business, can only be described as a loss of monies. Such a loss, it is contended, falls squarely within the purview of the exclusion clause, as a consequence of which the plaintiff is not entitled to make claim under the policy.

[39] In other words, as the plaintiff's claim relates directly to a loss of monies,

namely the sum of RM1,075,001.89, the defendant submits that the plaintiff is precluded or excluded by the proviso from making any claim by reason of the clear words of the exclusion clause.

[40] Additionally the defendant maintains that the payment of monies in the sum of RM1,075,001.89 by the plaintiff to the bank is a refund of an overcharged sum or premium as borne out by the official receipt issued by the bank. It states that the monies paid by the plaintiff are a refund of insurance premium overpaid. As these monies amount to 'overcharged premiums' this too does not fall within the terms of the policy.

[41] In support of its stance the defendant relies on a decision by the Supreme Court of Tasmania, namely *Rouleston Clarke Pty Ltd (In Liquidation) v FAI General Insurance Company Limited* [2000] TASSC 63. The case is of considerable relevance because the professional indemnity cover provided by the insurer is similar, if not almost identical to the words utilised in the instant policy. The rationale adopted by the Supreme Court of Tasmania is therefore germane to the instant case.

[42] The facts were as follows:

> The insurer issued a professional indemnity policy of insurance to the insured, which was at all material times carrying on a financial planning, investment advisory and tax agent's business and was a licensed dealer in securities. By clause 1(a) the insurer agreed to indemnify the insured against any claims for compensation for breach of professional duty in the conduct of its business by reason of any negligence committed by it or its employees. Exclusion clause (b) expressly excluded from the indemnity any claim against the insured for dishonest, fraudulent, criminal or malicious acts or omissions of the appellant or its employees except to the extent provided in those extensions to the policy for which the policy's schedule stated limits of indemnity. The extensions in this policy are therefore akin to the Optional Extensions in the Policy in the current suit.
>
> In the Tasmanian case, there were two (and not one) extensions, namely clause 4 which was for dishonesty up to a limit of $1 million (as per our case) and a second extension, namely clause 5, was for fidelity with a limit of $250,000-00. In effect therefore extension 4 which is comparable to Optional Extension Clause 1 in the instant case, had the same effect of negativing or deleting exclusion (b) so as to extend the terms and conditions of the policy to indemnify the insured in respect of claims for damages for breach of professional duty arising out of or contributed by the dishonest fraudulent, criminal or malicious conduct of employees.
>
> Extension 4 provided as follows:- 'If a limit for this extension is specified in the Schedule, Exclusion (b) is deleted and subject to the limitations, terms and conditions this Policy is extended to indemnify the Insured in respect of claims for damages for breach of professional duty arising out of or contributed by the dishonest, fraudulent, criminal or malicious conduct of employees, fellow partners

or co-directors. Provided that this Policy shall not provide indemnity to any person committing or condoning such dishonest, fraudulent, criminal or malicious act'.

This extension excludes claims for loss of money, negotiable instruments, bearer bonds or coupons, stamps, bank or currency notes. (Emphasis added.)

[43] It is therefore apparent that the extension cl 4 is similar to optional extension cl 1 in the instant case.

[44] An employee of the insured, one Peter Badger, converted to his own use negotiable instruments entrusted to him in his capacity as an employee of the insured, by 14 clients of the insured to a total value of $685,728.06. Disputes arose between the insured and the insurer as to the extent of the insurer's liability under the policy. One of the questions that arose for consideration was whether the insured was entitled to be indemnified for the claims it made pursuant to the dishonesty extension, ie cl 4 of the policy. The insured also sought to have answered the question of whether these same claims fell within the purview of the fidelity extension of the policy in cl 5:

The Fidelity Extension of the Policy provided as follows: "…… the Company will, subject to the limitations, terms and conditions, indemnify against any loss of money, negotiable instruments, bearer bonds or coupons, stamp, bank or currency notes

(a) Belonging to the Insured; or

(b) For which the Insured is or are legally liable

Which the Insured shall, during the period of cover discover that he or they have sustained in consequence to any dishonest or fraudulent act or omission of any employee, …… committed in the course of the business activities of the practice."

[45] The issue of whether the insured's claims fell within the dishonesty extension is on all fours with the instant case, given that the wording in the policies of these two cases is similar, particularly in relation to the exclusion clause.

[46] At first instance, the learned judge held that the insured was not entitled to be indemnified under the dishonesty extension by reason of the exclusion proviso to that extension. However it was held that the insured was entitled to be indemnified under cl 5, namely the fidelity extension (produced by way of footnote).

[47] The learned Judge at first instance concluded that he had no doubt that the indemnity provided by the insurer under cl 4 encompassed claims for the dishonest conduct of employees. As in the instant case, the insured there did

not dispute the fact that the acts of its employee were dishonest. However the insurer there relied on the proviso to the dishonesty extension (like the defendant here) to deny liability.

[48] The insured in that case contended that the word 'loss' in the proviso referred to physical loss and not loss in the sense of failing to account. That is similar to the position adopted by the plaintiff here. The insured in that case contended that the loss of the benefit of a negotiable instrument as a consequence of another person converting it to his use was not a loss within the meaning of that word in the proviso. In other words the insured contended that the proviso was only applicable where the instrument was physically lost. In other words it was contended that the proviso would only come into play where there was a loss of the actual physical instrument or monies, but not the benefit of the same. The insured submitted that the court should give the proviso a restricted meaning by reading or construing that the proviso related specifically to a physical loss of monies or negotiable instruments.

[49] The judge however disagreed contending, inter alia, that the proviso related to claims for damages for the loss of specified items. Such claims he reasoned, were only made where a financially measurable loss had been suffered. While the physical loss of some of the specified items, such as bank or currency notes would cause a financial loss such would not be the case with other negotiable instruments, which could be replaced with no financial loss. Given the scope of the proviso and the items specified there, he concluded that loss must mean more than just physical loss. The judge also considered the sort of conduct which gave rise to this loss, namely dishonest, fraudulent, criminal or malicious conduct of employees. While physical loss could arise from such conduct, the sort of loss which is more readily linked to this sort of conduct is detriment or disadvantage arising from the appropriation of specified items to the personal use of the employee. In other words financial loss was the most common sort of loss that tended to be suffered by reason of the conduct of dishonest employees.

[50] The judge then went on to consider the fidelity extension to conclude that that clause provided precisely for the loss suffered by the insured in the Tasmanian case, namely a loss of monies. The fidelity extension expressly provided cover for any loss of money. (However the limit of the cover was considerably less). The judge further reasoned that the words of the fidelity extension for loss of monies, negotiable instruments etc. intended that if any employee of the insured dishonestly appropriated any of the specified items to his use, the resultant loss to the insured would be covered. However if the meaning of the word 'loss' was confined to physical loss, then the insured would not be able to recover under the clause, as on the facts of the case the dishonest employee had converted a negotiable instrument to his own use,

rather than simply misappropriating the physical instrument. In other words a restricted approach to the words 'loss' to cover only physical loss would result in the insured having no cover even under the fidelity clause.

[51] As such he concluded that 'loss' could not be restricted to simply 'physical loss' for the purposes of the proviso to cl 4 either. It is evident from the reasoning of the learned judge that he considered the entirety of the insurance policy and concluded that the same meaning would have to be accorded to loss in the policy of insurance, albeit cll 4 or 5. If a restricted definition of loss, as advocated by the insured was adopted, so as to restrict 'loss' to physical loss and exclude financial loss, then the same meaning would have to be attributed to both cll 4–5. If so, then the insured could not recover under either clause because the clauses would only provide coverage or exclude coverage (as the case may be) for physical loss of monies or a negotiable instrument, but not for financial loss. This would have led to an unreasonable construction, which was therefore rejected.

[52] The conclusion was that the meaning of 'loss' as utilised in both the proviso to the dishonesty extension in cl 4 and the fidelity extension in cl 5 included detriment or disadvantage from being deprived of the benefit of any of the specified items regardless of whether they have been physically destroyed or mislaid.

[53] On the insured's appeal, the Supreme Court of Tasmania agreed with the reasoning of the learned judge at first instance. The insured argued, as does learned counsel for the plaintiff in the instant case, that the operative part of dishonesty extension in cl 4 has no work to do if loss for money, etc is given so wide a meaning as to encompass failures to account and claims for damages arising out of the fraudulent conduct of employees, instead of restricting it to the narrow meaning of physical loss. In other words the insured's grievance was that it could not hope to be indemnified at all under the policy for the dishonest acts of its employees, give the broad definition accorded to the phrase 'loss of monies' so as to extend it beyond mere physical loss. In nearly every instance, a dishonest act would give rise to financial loss, but by reason of the broad definition given to 'loss of monies' the insured would be deprived of cover.

[54] The Supreme Court addressed this submission by going on to consider the sorts of circumstances in which the insured could in fact recover under the policy notwithstanding the broad definition given to the word 'loss' so as to extend beyond physical loss. The examples were for example, an employee deliberately and maliciously causing a client to pay excessive tax (as the insured carried on the business of tax agents), or an employee dishonestly, fraudulently or maliciously inducing a client to invest money in a risky venture or upon a

false or misleading valuation. Or if the insured were in a business where the custody or care of the property of clients other than money or negotiable instruments was concerned, for example jewellery, it would be indemnified under the dishonesty extension of an employee fraudulently converted that property. The Supreme Court concluded that in that case the insured suffered a 'loss of money' when the fraudulent employee converted a client's cheque within the ordinary meaning of the expression in the proviso. 'Loss' was common expression insurance policies which was not limited to physical loss, but financial loss or damage.

[55] Learned counsel for the plaintiff in response to the defendant's submission of this case submitted that this court ought not to follow the Tasmanian case because:

(a) it is from a different jurisdiction. It was not binding and the reasoning ought not to be adopted;

(b) the case was distinguishable by reason of the existence of the fidelity extension in cl 5 which is absent here. The insured could recover under the fidelity clause which the insured here is deprived from doing;

(c) learned counsel instead urged that this court be guided by the general principles as enunciated by the Malaysian courts in *Perembun Consortium (a joint venture between Perembun (M) Sdn Bhd and Road Builder (M) Sdn Bhd) & Anor v AXA Affin General Insurance Bhd (fomerly known as AXA Affin Assurance Bhd)* [2011] 6 MLJ 719 and *Syarikat Uniweld Trading v The Asia Insurance Co Ltd* [1996] 2 MLJ 160. These cases are authority for the propostion that in interpreting any clause of an insurance policy, the commercial object or function of the clause is to be borne in mind, particularly its apparent relation to the contract as a whole. As stated by Malik Ishak J (now JCA): '… In adopting this approach, it becomes apparent that the literal meaning of the clause in the insurance policy must necessarily yield to business sense so that an ambiguity in the wording can be resolved';

(d) in other words it is contended that this court ought to give consideration to the policy as a whole, particularly its commercial or objective purpose which is to indemnify the insured against dishonest acts of its employees and therefore accord the proviso a construction which accords with this commercial or objective purpose. This would involve construing the word 'loss of monies' as 'physical loss of monies only'; and

(e) finally learned counsel also submitted that a construction of optional extension 1 as a whole, including the proviso ought to be read so as to mean that the insured was not covering instances where the risk insured against was a loss of monies. However it was effective where the consequence of a risk was the loss of monies. In other words, learned

counsel contended that in the instant case, the optional extension clause was effective in providing cover because the loss of monies suffered was a consequence of a risk that was covered. The proviso only operated to exclude cases where the risk was a loss of monies.

DECISION

[56] I have considered at some length the competing submissions of both counsel for the plaintiff and the defendant. At the outset, I was persuaded by the argument of learned counsel for the plaintiff that the optional extension clause would serve no useful purpose if the proviso to it were accorded its normal and natural meaning which would be to exclude financial loss, which was the loss suffered by the plaintiff in the instant case.

[57] Having gone through *Rouleston Clarke*'s case with a toothcomb however, I am satisfied to the contrary, namely that the proviso ought simply to be accorded its natural and ordinary meaning, so as to exclude loss of monies arising out of the dishonest acts of employees of the plaintiff.

[58] My reasons for so concluding are as follows:

(a) optional extension cl 1 certainly provides cover or indemnification for dishonest acts of the plaintiff's employees. However such cover is expressly subject to the proviso that it does NOT cover claims for loss of money, negotiable instruments, bearer bonds or coupons, stamps, bank or currency notes;

(b) as a result the question that arises for consideration is this: What is the construction to be accorded to the words 'claims for loss of money, negotiable instruments … etc'? The relevant words for the purposes of the instant case are 'loss of money'. Should the phrase be accorded a restricted definition, namely the loss of physical money only, or should it be accorded a broader construction so as to encompass financial loss etc. In this context I have considered and weighed the plaintiff's contention that the *contra proferentum* rule should be applied so as to construe the phrase in a restricted manner so as to give the entirety of optional extension 1 a meaning which is consistent with the commercial objective of the policy. The submission is that the plaintiff expressly purchased this policy to cover the dishonest acts of its employees. While this was initially an attractive proposition, it became considerably less so when the net effect and consequences of according such a limited meaning to the words 'loss of money' was considered in more detail;

(c) construing the phrase in the manner the plaintiff suggests requires this

court to effectively insert or read or construe into the proviso, the words 'physical' at the outset of the clause so as to limit the effect of the proviso to instances where there is a physical loss of money or a physical loss of negotiable instruments, bearer bonds or coupons. In other words the proviso is to be read as: 'This extension does not cover claims arising out or in connection with for *physical* loss of money, negotiable instruments …'. There appears to be no basis to justify the insertion of such a word so as to narrow or restrict the definition thus;

(d) if the parties had intended to cover only physical loss of monies or financial instruments, then this should have been and would have been clearly stipulated. There is a considerable difference between 'loss' and 'physical loss'. The latter envisages that the money or financial instrument is lost or misplaced or disappears. However 'loss' encompasses a wide variety of events including a shortfall or deficiency or debit or deficit of money albeit from theft of monies or loss of a financial benefit by reason of the loss of a financial instrument, rather than the physical loss of the instrument itself. Loss also routinely encompasses damage and injury in a variety of insurance policies. Given the wide discrepancy between the definitions, it would have been incumbent upon parties to specify that loss was restricted to a physical loss;

(e) the insertion of the word 'physical' cannot be justified as an 'implied' term under the commercial necessity test or the official bystander test;

(f) l turn to learned counsel for the plaintiff's submission that the proviso should be read such that it excludes claims where the risk insured against is a loss of monies, rather than a situation as in the present case where the consequence of the risk is the loss of money. If the policy is read as a whole it will be noted at the outset under the exclusions clause that the defendant expressly excludes indemnity for dishonesty in 1(b) and separately for loss of money in cl 1(d). Clause 1(d) provides that there is no indemnity for loss of money, negotiable instruments, bearer bonds, coupons stamps, bank or currency notes in the care or custody of the insured. It sets out the risk which the defendant expressly excludes.

The proviso to the dishonesty extension in optional extension 1 however provides simply that the defendant will not indemnify the plaintiff for claims arising out of loss of money, negotiable instruments etc. The words 'in the care or custody of the insured' do not appear.

As such it appears to this court that the proviso to optional extension 1 does not refer to a risk as is contended by the plaintiff, but instead refers to the consequence of the occurrence of a risk where the risk is the dishonest conduct of an employee;

(g) when read as a whole this policy provides indemnity for claims for damages arising out of a breach of professional duty. Here there is a claim for damages or loss suffered as a consequence the acts of a dishonest

employee. Claims for damages are made where a financially measurable loss has been suffered. This too, to my mind, suggests that the word 'loss' in the proviso must be given a meaning wider than simply 'physical loss';

(h) in conclusion the word 'loss' ought to be accorded its natural and ordinary meaning. There is no basis to construe it so as to include the word 'physical'. To do so would be to give it a strained construction to meet the facts of the instant case. This is particularly so, given that the word 'loss' is routinely utilised in insurance policies to encompass a wide variety of matters from financial deficit to injury and harm. It is regularly utilised to designate financial loss or damage;

(i) in the instant case Razak fraudulently induced the bank to part with money for fraudulent purposes. The bank lost money. Ultimately money was diverted from the plaintiff's custody to a third party's account to allow Razak to misappropriate the same. The money that was lost was the bank's money. The bank and ultimately the plaintiff suffered financial loss. The clause here indemnifies the insured plaintiff against dishonest conduct of its employees but not where financial loss has been suffered. A fidelity type option would have to be separately purchased for coverage for loss of monies; and

(j) as pointed out in *Rouleston Clarke*'s case the proviso would cover instances where an employee fraudulently induces a client to procure insurance cover when aware that there could be no coverage under that policy.

[59] I therefore conclude by answering question 1 as follows:

> The loss of monies claimed by the plaintiff as a result of the (fictional) Risk Management Programs does not fall within the Optional Extension Clause of the Policy. Question 1 is therefore answered in the negative.

Question 2: Whether the payments to the individual event management companies falls within the optional extension clause of the policy

[60] This question relates to the second tranche of the modus operandi assumed by Razak in diverting the monies paid by the bank to the plaintiff into third party accounts to which he had direct access, thereby entitling him to take the monies for his own use. The plaintiff contends that these payments do fall within the optional extension clause of the policy and that this question should also be answered in the affirmative. To a large extent the arguments canvassed in question 1 will be applicable here.

[61] Ultimately whether the loss is considered as having arisen at the point when the bank made the payments to the plaintiff or the monies were diverted from the plaintiff into third party accounts by the dishonest machinations of

Razak, the loss is a financial loss. The financial loss was suffered by the bank and was reimbursed by the plaintiff. This claim is therefore a claim arising from financial loss suffered by a client in respect of which it sought reimbursement from the plaintiff as the financial loss arose by reason of the dishonest acts of the plaintiff's employee. However it cannot be disputed that at all times the basis of the claim was a loss of monies brought about by the dishonest conduct of Razak.

[62] Given the analysis of the matter in question 1 above, it follows that these payments to the individual event management companies which was part of the fraud or modus operandi utilised by Razak, fall within the proviso to optional extension clause 1, being a loss of monies.

[63] I therefore adopt my reasoning in relation to question 1 above and conclude that the transmission of these monies to the third party event management companies also amounts to a loss of money within the proviso to the extension and therefore do not attract any cover. Question 2 is answered in the negative.

[64] As questions 3–4 are no longer in issue there is no requirement to consider the same.

[65] The plaintiff's claim is therefore dismissed.

Claim dismissed.

Reported by Afiq Mohamad Noor